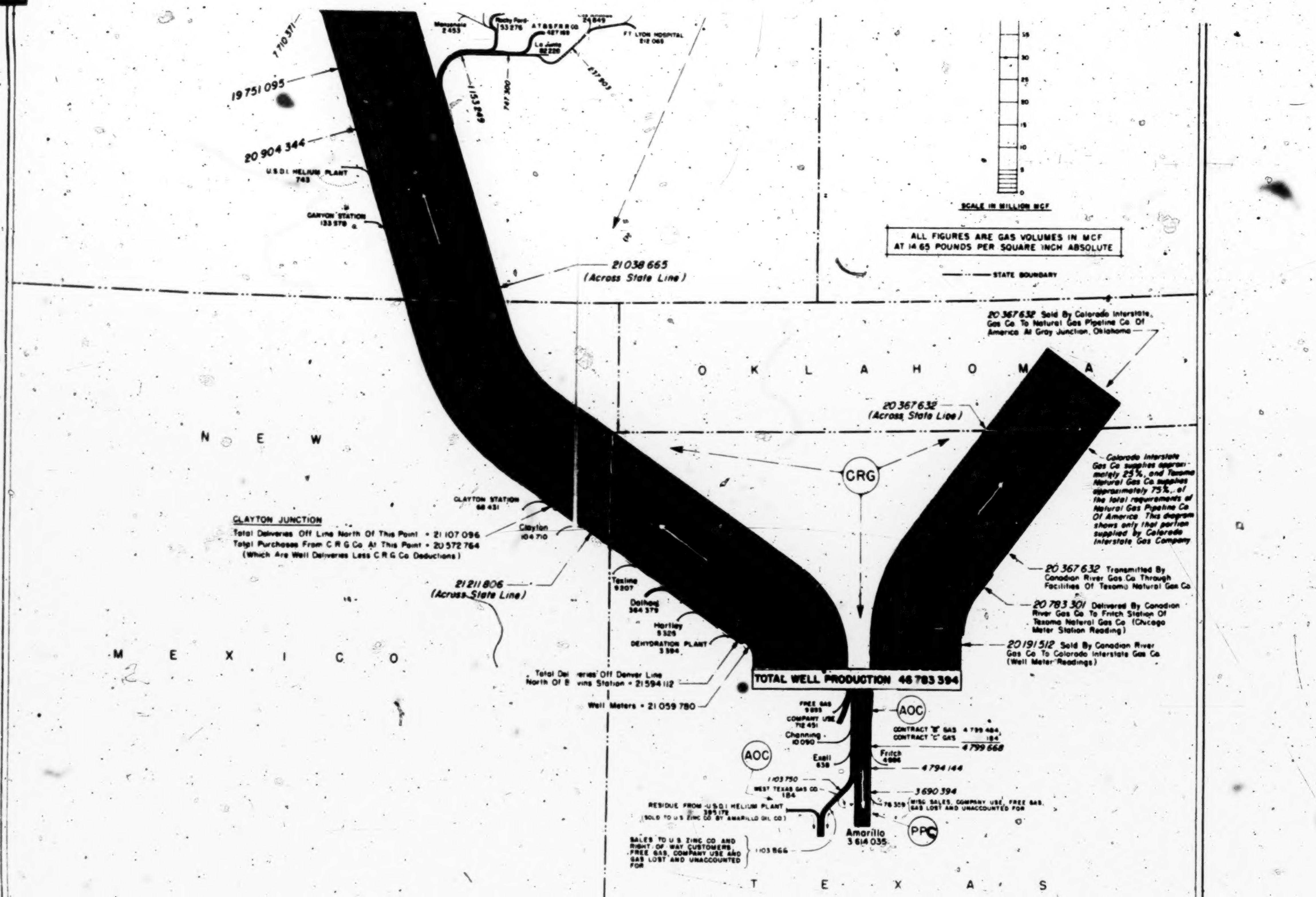

Manzanola 2 453
Rocky Ford 53 276
A T & S F R R CO 427 169
La Junta 82 226
24 849
FT LYON HOSPITAL 212 069
1 710 371
19 751 095
20 904 344
1 153 849
747 300
237 903
U S D I HELIUM PLANT 743
CANYON STATION 133 579
SCALE IN MILLION MCF
ALL FIGURES ARE GAS VOLUMES IN MCF AT 14 65 POUNDS PER SQUARE INCH ABSOLUTE
STATE BOUNDARY
21 038 665 (Across State Line)
20 367 632 Sold By Colorado Interstate Gas Co To Natural Gas Pipeline Co Of America At Gray Junction, Oklahoma
O K L A H O M A
20 367 632 (Across State Line)
N E W
M E X I C O
CRG
Colorado Interstate Gas Co supplies approximately 25%, and Texoma Natural Gas Co supplies approximately 75%, of the total requirements of Natural Gas Pipeline Co Of America. This diagram shows only that portion supplied by Colorado Interstate Gas Company
CLAYTON STATION 68 431
CLAYTON JUNCTION
Total Deliveries Off Line North Of This Point = 21 107 096
Total Purchases From C R G Co At This Point = 20 572 764
(Which Are Well Deliveries Less C R G Co Deductions)
Clayton 104 710
21 211 806 (Across State Line)
Texline 9 207
Dalhart 364 379
Hartley 5 325
DEHYDRATION PLANT 3 394
20 367 632 Transmitted By Canadian River Gas Co Through Facilities Of Texoma Natural Gas Co
20 783 301 Delivered By Canadian River Gas Co To Fritch Station Of Texoma Natural Gas Co (Chicago Meter Station Reading)
20 191 512 Sold By Canadian River Gas Co To Colorado Interstate Gas Co (Well Meter Readings)
Total Deliveries Off Denver Line North Of Bivins Station = 21 594 112
Well Meters = 21 059 780
TOTAL WELL PRODUCTION 46 783 394
FREE GAS 9 893
COMPANY USE 712 451
Channing 10 090
AOC
CONTRACT "B" GAS 4 799 484
CONTRACT "C" GAS 184
4 799 668
Exell 638
Fritch 4 986
4 794 144
1 103 750
WEST TEXAS GAS CO 184
3 690 394
76 359 MISC SALES, COMPANY USE, FREE GAS, GAS LOST AND UNACCOUNTED FOR
RESIDUE FROM U S D I HELIUM PLANT 395 172 (SOLD TO U S ZINC CO BY AMARILLO OIL CO)
SALES TO U S ZINC CO AND RIGHT OF WAY CUSTOMERS, FREE GAS, COMPANY USE AND GAS LOST AND UNACCOUNTED FOR 1 103 866
Amarillo 3 614 035
PPC
T E X A S

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Natural Gas Act of 1938, c. 556, 52 Stat. 821 (15 U. S. C. 717, *et seq.*):

In the Supreme Court of the United States

OCTOBER TERM, 1944

NOS. 379 AND 380

COLORADO INTERSTATE GAS COMPANY, A CORPORATION, PETITIONER

v.

FEDERAL POWER COMMISSION, CITY AND COUNTY OF DENVER, COLORADO, PUBLIC SERVICE COMMISSION OF WYOMING, COLORADO-WYOMING GAS COMPANY, PUBLIC SERVICE COMPANY OF COLORADO, AND CANADIAN RIVER GAS COMPANY

CANADIAN RIVER GAS COMPANY, A CORPORATION, PETITIONER

v.

FEDERAL POWER COMMISSION, CITY AND COUNTY OF DENVER, COLORADO, PUBLIC SERVICE COMMISSION OF WYOMING, COLORADO-WYOMING GAS COMPANY, PUBLIC SERVICE COMPANY OF COLORADO, AND COLORADO INTERSTATE GAS COMPANY

ON PETITIONS FOR WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE TENTH CIRCUIT

BRIEF FOR THE FEDERAL POWER COMMISSION, CITY AND COUNTY OF DENVER, COLORADO, AND PUBLIC SERVICE COMMISSION OF WYOMING, IN OPPOSITION

OPINIONS BELOW

The opinion and orders of the Federal Power Commission (R. I, 140–192) are reported in 43 P. U. R. (N. S.) 205. The opinion of the circuit court of appeals (R. VIII, 5066–5094) is reported in 142 F. (2d) 943.

JURISDICTION

The judgment of the circuit court of appeals was entered July 8, 1944 (R. VIII, 5094). The petitions for writs of certiorari were filed on August 22, 1944. Jurisdiction of this Court is invoked under Section 19 (b) of the Natural Gas Act, and Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

1. Whether the Commission, in determining Canadian's rate base, properly disallowed that portion of Canadian's claimed cost of gas producing properties and leaseholds which was found to consist of profits obtained by Canadian's affiliates; and, in determining Colorado's rate base, properly disallowed the amounts claimed as cost to Colorado of certain gas purchase and sale contracts, which amounts were also found to be intercompany profits.

2. Whether the Commission's findings with respect to Canadian's gas reserves are supported by substantial evidence.

3. Whether the allocations of cost made by the Commission between petitioners' intrastate and direct industrial sales, and their interstate sales for resale, are appropriate.

4. Whether the rates prescribed for petitioners are confiscatory.

STATUTES INVOLVED

The applicable portions of the Natural Gas Act are set forth in the Appendix, *infra*, pp. 23–27.

STATEMENT

The proceedings before the Commission arose out of a complaint filed on December 22, 1938, by the City and County of Denver, Colorado, against Public Service Company of Colorado, and petitioners, Colorado Interstate Gas Company ("Colorado") and Canadian River Gas Company ("Canadian"), alleging that the rates charged by Colorado for natural gas purchased from Canadian and sold to Public Service Company of Colorado for resale in Denver were excessive, unreasonable, unjust, and discriminatory (R. I. 302). On January 9, 1939, the Public Service Commission of Wyoming filed a complaint with the Commission alleging that the rates of Canadian and Colorado for natural gas sold to Colorado-Wyoming Gas Company for resale to Cheyenne Light, Fuel and Power Company, which distributes such gas in Cheyenne, Wyoming, were unjust, unreasonable, and discriminatory (R. I. 333). The Commission,

on its own motion, instituted an investigation, on March 14, 1939, of all interstate wholesale rates and charges of petitioners, Colorado and Canadian, and of Colorado-Wyoming Gas Company (R. I, 317).[1]

Hearings on the complaints and the investigation were consolidated by the Commission, begun on October 28, 1940, and held on 102 days (R. I, 141). After submission of briefs, the Commission, on March 18, 1942, issued its opinion and orders here under review, finding that the interstate wholesale rates of Canadian were excessive by $561,000 per year and those of Colorado by $2,065,000 per year, and requiring petitioners to reduce such rates accordingly (R. I, 185–192).[2] The following facts, found by the Commission, are clearly established by the evidence:

The Petitioners.—Canadian and Colorado were incorporated and financed, and are operated pursuant to an agreement dated April 5, 1927, between

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[1] On April 12, 1939, petitioners filed with the Commission a joint application praying for a stay of the order instituting the investigation, which the Commission denied by order dated May 9, 1939. A petition to review the latter order was dismissed by the Circuit Court of Appeals for the Tenth Circuit in *Canadian River Gas Company, et al.* v. *Federal Power Commission*, 110 F. (2d) 350, rehearing denied, 113 F. (2d) 1010, certiorari denied, 311 U. S. 693.

[2] Canadian's reduction includes $551,000 which is applicable to its sales to Colorado, and the portion of this amount allocated to Colorado's interstate sales for resale is included in the $2,065,000 reduction prescribed for Colorado (R. I, 176, 177).

Southwestern Development Company ("Southwestern"), Standard Oil Company (N. J.) ("Standard") and Cities Service Company ("Cities Service") (R. I, 381–401). By this agreement Southwestern, Standard and Cities Service pooled their respective gas reserves, finances and distribution markets, to bring natural gas from the Panhandle field to the Denver and Pueblo, Colorado, markets. This pooling was effected in the following manner:

Southwestern, through a wholly owned subsidiary, Amarillo Oil Company ("Amarillo"), controlled certain gas leaseholds and producing properties in the Texas Panhandle field, which Southwestern agreed to transfer to a new subsidiary (Canadian) which it would organize for that purpose (R. I, 381–382). Standard agreed to form a new corporation (Colorado) and to finance its construction of pipeline facilities to connect with and transport gas from Canadian's facilities to the Denver market and intermediate points including Pueblo (R. I, 385). Cities Service was to procure franchises through its subsidiaries under which such natural gas could be distributed in Denver and Pueblo (R. I, 391). It was agreed that Canadian would sell gas to Colorado at "cost" for at least 20 years from 1928, such "cost" to include amortization of all of Canadian's indebtedness over the twenty-year period and to be decreased by any profits Canadian might obtain from other sources, including local

sales permitted by Colorado (R. I, 392; R. II, 719–732). Canadian, under the "cost" contract, would have nothing available for dividends on its common stock during the first 20 years (R. III, 1436) and so long thereafter as Colorado might choose to purchase its gas at "cost" (R. III, 1435).

Pursuant to the agreement, Southwestern organized Canadian to which were transferred the gas leaseholds and producing properties of Amarillo, also a wholly-owned subsidiary of Southwestern. The cash consideration for this transfer was $5,000,000, stipulated in the tripartite agreement, and advanced by Standard for this purpose at 6% interest (R. I, 392, R. V, 2936–2937).[3] To repay the advance and to finance the acquisition and construction of additional facilities, Canadian issued $11,000,000 of twenty-year 6% sinking fund bonds, which Colorado purchased from the proceeds of its $19,200,000 of twenty-year 6% sinking fund bonds, which, in turn, were purchased by Standard, in accordance with the 1927 agreement (R. I, 496).

As had been further agreed, Standard organized Colorado with $2,000,000 par value of 6% preferred stock and 1,250,000 shares of no par common stock, and paid $1,000,000 in cash for half of the preferred stock and another $1,000,000 in

[3] As hereinafter discussed, *infra*, pp. 12–13, the Commission, in determining Canadian's rate base, disallowed the $3,249,030 portion of this amount which was in excess of the $1,750,970 cost of such properties to Amarillo and its affiliates.

cash for its portion (42½%) of Colorado's common stock (R. II, 626). Southwestern (as nominee of Canadian) also received half of Colorado's preferred stock and 42½% of the common stock (R. II, 626), the remaining 15% of the common stock being issued to Cities Service (R. I, 395–396, R. II, 627). It was implicit in the tripartite agreement, therefore, that Southwestern, Standard, and Cities Service would receive their profits from the operations of the enterprise by way of dividends on Colorado's stock.

The preferred stock was recorded on Colorado's books at the par value of $2,000,000 and the no par common stock (1,250,000 shares) was recorded at $2,352,941.17, based on what Standard had paid in cash for its 42½% (531,250 shares) of such stock (R. II, 627). These entries were balanced by charges to Colorado's asset accounts totalling $4,352,941.17 (R. II, 626, 627; R. III, 1427).[4]

The Commission's Orders.—In requiring Canadian to reduce its interstate wholesale rates by $561,000 annually, the Commission found the actual legitimate cost of the Company's plant at December 31, 1939, to be $10,784,464 (R. I, 186).

[4] As hereinafter discussed, *infra*, pp. 11–12, the Commission, in determining Colorado's rate base, disallowed the $2,352,941.17 portion of this amount (R. I, 152), which was in excess of the $2,000,000 which Standard paid in cash for its share of Colorado's preferred and common stock.

From this amount it deducted $2,134,629 for accrued depreciation and depletion as of that date, and added $150,738 for working capital and $571,923 covering gross plant additions to December 31, 1941. This resulted in a rate base of $9,372,496, which was rounded to $9,375,000 (R. I, 187). In requiring Colorado to reduce its interstate wholesale rates by $2,065,000 annually, the Commission found the actual legitimate cost of the company's plant at December 31, 1939, to be $11,879,409 (R. I, 190). From this amount it deducted $2,793,410 for accrued depreciation and amortization as of that date; and added $109,065 for working capital and $337,000 covering gross plant additions to December 31, 1941. This resulted in a rate base of $9,532,064, which was rounded to $9,535,000 (R. I, 190). Petitioners' estimates of reproduction cost were considered by the Commission and were found to be too conjectural to have probative value (R. I, 148). The Commission further found that actual costs, which could be readily determined from petitioners' accounting records, represented the best and only reliable evidence as to rate base (R. I, 148).

The Commission allowed a $6\frac{1}{2}\%$ return on the rate base of each petitioner, which return it found to be "fair and reasonable" (R. I, 187, 190), noting that Colorado in 1940 had refinanced its outstanding bonded indebtedness at an interest rate of $2\frac{3}{4}\%$ (R. I, 173). With certain minor

exceptions, the Commission allowed each petitioner the taxes, operating expenses, exploration and development costs, shown by its books for the test year, 1939, adjusted to reflect accrual accounting (R. I, 166–169; R. VI, 3387). The Commission also allowed amounts to amortize rate case expenses over a five-year period (R. I, 166, 168). Annual allowances for depreciation, depletion and amortization were determined on the basis of the economic service lives of petitioners' properties,[5] such allowances being consistent with the amounts deducted for accrued depreciation, depletion and amortization in arriving at the rate bases (R. I, 160, 156). The Commission found that, based on the present and expected future rate of production, Canadian's gas reserves would last 53 years after 1939 (R. I, 159), and rejected, as not supported by any reliable evidence, petitioners' contentions that the enterprise would have to be abandoned by 1956 (R. I, 160).

In arriving at the amount of the reductions in the interstate wholesale rates, the Commission made an allocation of the cost of service of each petitioner, including in such cost the fair return on the rate base, and determined the excess of revenues over costs for intrastate sales, direct industrial sales, and interstate sales for resale (R. I, 176–177).

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[5] Depletion of Canadian's production properties was computed by the unit-of-production method based on its recoverable gas reserves (R. I, 160).

The petitioners, on April 14, 1942, applied for a rehearing and stay of the Commission's orders (R. I, 203, 238, 277, 284), and on May 13, 1942, the Commission issued its supplemental opinion and orders denying such petitions (R. I, 296–301). Thereafter, petitions for review were filed in the Circuit Court of Appeals for the Tenth Circuit, which heard argument on September 14–15, 1943, handed down its opinion on May 16, 1944, and entered its judgment on July 8, 1944, affirming the Commission's orders (R. VIII, 5065–5094).

ARGUMENT

In any rate proceeding, and particularly in cases such as these which involve an enterprise with unusually complicated intercompany arrangements, errors can readily be alleged and controversies arise in respect of many of the adjustments which the Commission may be compelled to make in determining just and reasonable rates. We submit that the only issues posed by the numerous questions raised in the petitions which are of significance at this stage of the proceedings are the Commission's elimination of intercompany profits from the rate bases, the sufficiency of the evidence to support the findings as to gas reserves, the method of allocation, and the question of confiscation.

1. *The Commission properly eliminated the intercompany profits from the rate bases of Canadian and Colorado.*—As has already been noted,

Southwestern, Cities Service and Standard, acting under the 1927 agreement, pooled their respective gas reserves, distribution markets and finances, and agreed upon an apportionment of the profits of the joint enterprise. Standard paid $2,000,000 in cash for its half of Colorado's preferred stock and its 42½% of the common stock (R. II, 626). This equity capital was reflected in Colorado's rate base and accordingly allowed by the Commission. But neither Southwestern nor Cities Service paid any cash consideration for their portions of Colorado's stocks (R. II, 628). The preferred stock (50%) and the common stock (42½%) issued to Southwestern was recorded on Colorado's books at $2,000,000 and the common stock (15%) issued to Cities Service was recorded at $352,941.17 (R. II, 627). The book value thus assigned to this stock was based upon what Standard had paid in cash for its portion (R. II, 627), and was balanced by a $2,352,941.17 charge to Colorado's plant accounts (R. III, 1749). This charge, which was recorded as "Cost of Contracts" (R. II, 628), did not represent any investment of cash or tangible property in the enterprise and was properly disallowed by the Commission, which realistically recognized it as promoters' profit. Cf. *Northwestern Electric Company* v. *Federal Power Commission*, 321 U. S. 119. Moreover, any arm's length bargaining between the parties to the 1927 agreement was

limited to the division of profits to be effected through the distribution of Colorado's stock. *Niagara Falls Power Company* v. *Federal Power Commission*, 137 F. (2d) 787, 793–794 (C. C. A. 2), certiorari denied, 320 U. S. 792.

Similarly, with respect to the $5,000,000 of cash allotted to Southwestern under the agreement, the court below properly affirmed the Commission's disallowance of the $3,249,030 portion thereof which was found to be in excess of actual cost to Amarillo and its affiliates (R. I, 150). There is no merit in Canadian's contentions that Southwestern's transfer of these properties, in accordance with the 1927 agreement, from one wholly-owned subsidiary (Amarillo) to another (Canadian), constituted a purchase and sale, or that the $5,000,000 represented the purchase price agreed upon "after prolonged arm's-length bargaining" (Can. Pet. 18). On the contrary, the record shows that this allotment of cash was made to Southwestern because of its poor financial condition (R. I, 520, 559) and was as much a part of Southwestern's share in the profits of the joint enterprise as its allotment of Colorado's stock (R. I, 392). The $5,000,000 was actually paid by Standard directly to Prairie Oil and Gas Company, a holding company affiliated with Southwestern, and was used by Prairie in discharging certain obligations of Southwestern and Amarillo, in advancing $1,000,000 to West

Texas Gas Company, and in furnishing $310,000 to Amarillo (R. V, 2937, 2932–35). Canadian was not formed until after the $5,000,000 had been paid, and, significantly, none of the companies involved paid any income tax as a result of the so-called "sale" (R. V, 2936, 2638). The intercompany profit which disappeared on the consolidated tax return of Southwestern and its subsidiaries, including Amarillo and Canadian, "is too lacking in substance to be treated as an actual cost." *Pennsylvania Power & Light Company* v. *Federal Power Commission,* 139 F. (2d) 445, 450 (C. C. A. 3), certiorari denied, 321 U. S. 798. Moreover, until 1939, Canadian carried the intercompany profit on its books as "Appreciation".[6] (R. V, 2630–2632).

The "no profits to affiliates" rule, which the Commission here applied, precludes any allowance in the rate bases for the items in question. The propriety, as well as the constitutionality, of the Commission's action in enforcing the rule has been before the courts on numerous occasions, and has uniformly been upheld. *Alabama Power Company* v. *McNinch,* 94 F. (2d) 601, 608, 615, 618 (App. D. C.); *Alabama Power Company* v. *Federal Power Commission,* 128 F. (2d) 280, 284

[6] The Commission's Uniform System of Accounts under the Natural Gas Act (p. 17), like that prescribed under the Federal Power Act (p. 19), does not permit the recording of appreciation in the plant accounts. *Northwestern Electric Company* v. *Federal Power Commission,* 321 U. S. 119.

(App. D. C.), certiorari denied, 317 U. S. 652; *Alabama Power Company* v. *Federal Power Commission*, 134 F. (2d) 602, 609 (C. C. A. 5); *Puget Sound Power & Light Co.* v. *Federal Power Commission*, 137 F. (2d) 701, 703 (App. D. C.); *Niagara Falls Power Company* v. *Federal Power Commission*, 137 F. (2d) 787, 793–794 (C. C. A. 2), certiorari denied, 320 U. S. 792; *Pennsylvania Power & Light Co.* v. *Federal Power Commission*, 139 F. (2d) 445, 450 (C. C. A. 3), certiorari denied, 321 U. S. 798.

2. *The Commission's allowances for depreciation and depletion are adequate.*—The principal controversy in respect to depreciation and depletion arises from the Commission's finding that Canadian's gas reserves have an estimated life of 53 years from 1939. Canadian contends that because of drainage by other wells in the Panhandle field, its reserves will be exhausted within 27 years from 1939, which it now claims to be the maximum life of the Panhandle field as a whole. Canadian further contends that the Commission ignored the question of drainage and thus erred as a matter of law (Pet. 36–37). We submit that these contentions are without merit.

The Commission is entitled to evaluate the evidence and to draw rational inferences therefrom, and the finding by the Commission that Canadian's gas reserves had a potential life of 53 years clearly has ample support in the record.

The Commission's expert calculated the recoverable reserves by the "pressure decline method," the soundness of which was recognized by this Court in *Dayton Power and Light Company* v. *Commission*, 292 U. S. 290, 306, and testified that on an assumed annual withdrawal of fifty billion cubic feet, Canadian's remaining reserves would last 73.7 years (R. VI, 3628–3629). The Commission considered Canadian's objections to this estimate, which included the contention that "account was not taken of the migration of gas under Canadian's acreage," and noted that theoretically such migration is automatically accounted for under the "pressure decline method" and is actually accounted for if the iso-baric maps are properly drawn (R. I, 158–159).

As the lower court properly held, "it nowhere appears that the Commission failed appropriately to weigh" the "existing volume, pressure differentials and consequent drainage, and other recovery factors" (R. VIII, 5091). The lower court also observed that the determination of Canadian's recoverable reserves necessarily involved "specialized and technical factors," as to which the informed judgment of the Commission, when supported by substantial evidence, should be controlling [Secs. 9 (a) and 19 (b) of the Act, *infra*, pp. 25–27] (R. VIII, 5092).

Moreover, as pointed out by the Commission in its opinion, "it makes little difference whether the

service life principle based on the longer expected life, or the company's amortization principle based upon a 1956 expiration, is adopted. The net results as to excess earnings are substantially the same, provided consistency is maintained in computing the annual expense and the accrued depreciation and depletion reserve requirement" (R. I, 160). As the lower court properly held, "there is no basis in this record on which it can be concluded that the determination of depreciation in the manner adopted by the Commission will result in any of these orders in its entirety causing a failure to restore the capital investment at the end of the term, and therefore no deprivation of property is involved" (R. VIII, 5089).

Certain incidental contentions which petitioners advance in this connection may be dealt with briefly. Canadian contends (Pet. 25) that it will be required to invest $6,500,000 in future replacements and Colorado contends (Pet. 23) that the depreciation allowance made to it will be inadequate to amortize future replacements. As this Court ruled in *Federal Power Commission* v. *Natural Gas Pipeline Company,* 315 U. S. 575, 587, n. 5 "the refusal to include in the rate base capital expenditures not yet made can not involve confiscation." It follows that amortization of such expenditures is likewise not required.

3. *The cost allocations made by the Commission are appropriate.*—Both Canadian and Colorado contend that the allocations of costs which the Commission made between regulable and non-

regulable sales did not comply with the jurisdictional requirements in Section 1 (b) of the Act (Appendix, *infra*, p. 23). Canadian's principal objection is that the Commission had no jurisdiction to reduce its charges to Colorado for gas which the latter resells directly to industrial customers (Pet. 27). An adequate answer to Canadian's view that such reduction "serves no useful purpose" (Pet. 39), is that the Act specifically applies to its interstate sales for resale "for domestic, commercial, *industrial*, or any other use" (Sec. 1 (b)). Moreover, the absence of jurisdiction over Colorado's direct industrial rates was recognized by the Commission, and only that portion of the annual reduction in Canadian's rates to Colorado properly allocable to Colorado's interstate sales for resale was reflected in the annual reduction prescribed for Colorado (R. I, 176, 177).

Colorado advances the contention (Pet. 23–30), in which Canadian joins (Pet. 40), that the Commission instead of making a determination of costs properly chargeable against the regulable sales, was required to make an allocation of property (Colo. Pet. 11). We submit that this contention is without merit. The decisions cited by Colorado (Pet. 24–28) cannot be read as precluding a federal administrative judgment as to the best method of allocation under the circumstances of a particular case. The Natural Gas Act does not prescribe any method of allocation, or even require

that any formal allocation be made. As the Commission noted, Canadian and Colorado failed to make a complete presentation of their entire operations "broken down between jurisdictional and non-jurisdictional operations." The Commission found that "all that can be accomplished by an allocation of physical properties can be attained by allocating costs including the return" (R. I, 175). This method, which the Commission termed "by far the most practical and business-like" (R. I, 175), was described in its opinion as follows: "* * * costs are divided essentially into two groups, fixed and variable. Fixed costs are largely joint costs which do not vary with volume of sales. The total amount of such costs are largely proportional to the maximum demand on the system or system capacity. Accordingly, these costs have been allocated basically in proportion to each customer's responsibility for the peak day demand. Variable costs are largely those that vary proportional to output or volume of sale. Accordingly, these costs have been allocated in proportion to volume of gas purchased by each customer." (R. I, 175-176). We submit that this method of allocation was, as the lower court observed, "a working one suitably adapted to the particular circumstances" (R. VIII, 5087).[7]

[7] Canadian's contention that by finding the cost of its facilities employed in the production and gathering of natural gas the Commission exceeded its jurisdiction under Section 1 (b) of the Act is without merit. Canadian's sales at wholesale in

4. ***The Commission's orders do not involve confiscation.***—Canadian contends that any reduction in its rates is confiscatory because its contractual obligation to sell gas to Colorado at "cost" precludes any possibility of its making a profit under its existing rates (Pet. 19–20). But the alleged "cost" under the contract includes the amortization of Canadian's entire indebtedness [representing all its capital except its common stock issued for $1.00 (R. II, 688)] over a twenty-year period, which is admittedly much less than the life of the enterprise. Thus, to the extent that such amortization exceeds proper depreciation and depletion,[8] Canadian is necessarily making substantial profits on which it has been required to pay an income tax (R. III, 1745). The fact that Colorado did not obligate itself under the contract to purchase Canadian's gas beyond the twenty-year period, and thus made it desirable for Canadian to amortize all its costs within that period, is no longer of any

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interstate commerce are subject to regulation under the Act. The Commission was required to fix rates that are just and reasonable. This it would be unable to do if it were not in a position to ascertain the rate base upon which to determine the reasonableness of the rates charged and, in order to determine the rate base, it was necessary to consider the production and gathering facilities. A ~~similar~~ similar argument was summarily rejected by this Court in *Federal Power Commission v. Hope Natural Gas Company*, 320 U. S. 591, 614, n. 25.

[8] At the end of the test year, 1939, Canadian's "cost" of gas under the contract had included amortization of debt totaling $9,073,565 (R. VI, 3581). The Commission deducted $2,134,629 for depreciation and depletion in finding Canadian's rate base (R. I, 161).

significance, since neither Colorado nor Canadian can abandon its interstate facilities or service without the prior approval of the Commission. Sec. 7 (b)). The contractual prohibition against Canadian's sale of gas without the consent of Colorado is likewise subject to the Commission's authority to require extensions of service (Sec. 7 (a)). Canadian complains, however, that it is left with the obligation of the contract without the ability to collect the income it will need thereunder (Pet. 33). The answer to this contention is to be found in *Chicago, B. & Q. R. R. Co.* v. *Iowa*, 94 U. S. 155, 162–163, where this Court held in a rate proceeding, that it was immaterial that the company, prior to regulation, "had pledged its income as security for the payment of debts incurred, and had leased its road to a tenant that relied upon the earnings for the means of paying the agreed rent."

Nor does the financial history of the enterprise sustain the validity of a "confiscation" argument on the part of Colorado or Canadian. All of the properties of both Colorado or Canadian were acquired or constructed with the proceeds of loans, with the exception of $2,000,000 of equity capital invested by Standard. Colorado by December 31, 1939, had paid dividends totalling $8,005,000 (R. III, 1691) and accumulated a depreciation reserve of $4,994,352.35, a reserve for amortization of contracts of $1,471,546.15, and an undistributed surplus of $2,479,133.92 (R. III,

1711). Moreover, by that date, Colorado's outstanding debt had been reduced to $8,865,000 represented by bonds (R. III, 1711), the interest on which was reduced to 2¾% in 1940 (R. II, 632). Canadian's financial condition is comparable. Its claimed "total cash investment" in plant of $15,220,744 at December 31, 1941, had been recovered, except for $4,368,703, in the "cost" of gas by December 31, 1941 (R. VI, 3581). The Commission's allowance of $838,157 for annual depreciation, depletion and return on plant (R. I, 171, 173), thus represents approximately 20% of Canadian's unrecovered claimed investment. We submit that under these circumstances there is no confiscation. See *Federal Power Commission v. Natural Gas Pipeline Company*, 315 U. S. 575, 578-579, and *Federal Power Commission v. Hope Natural Gas Company*, 320 U. S. 591, 603-606.[9]

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[9] Canadian's objections to the amount of revenues found available for return are similarly predicated upon the "cost" contract (Pet. 22-23). Contrary to the implication in the petition (p. 23), the Commission's accountant restated Canadian's revenues, as well as its expenses, during the test year on an accrual basis (R. VI, 3387). Canadian's contention that its revenues were overstated is accordingly based on the provision in the "cost" contract that any reduction in Canadian's costs necessarily reduces its rates to Colorado. Similarly, the $13,056.24 adjustment for profits to an affiliate in connection with extraction of gasoline (Pet. 23) was allocated exclusively to sales to Amarillo Oil Company at the wells (R. IV, 2317, 2382), and these rates were not affected by the Commission's order. Canadian's contentions with respect to the $26,350 increase in the Texas gross production

CONCLUSION

The decision below is correct and there is no conflict. We respectfully submit that the petitions for writs of certiorari should be denied.

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SEPTEMBER 1944.

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taxes (Pet. 24) were first raised in its brief in the court below. This amount, in any event, is more than offset by the Commission's allowance of $66,403 for Federal income tax for which there appeared to be no liability if Canadian's return were limited to that found fair and reasonable by the Commission (R. I, 297).

APPENDIX

The pertinent provisions of the Natural Gas Act of 1938, c. 556, 52 Stat. 821 (15 U. S. C. 717 *et seq.*), are as follows:

> SEC. 1. (b) The provisions of this Act shall apply to the transportation of natural gas in interstate commerce, to the sale in interstate commerce of natural gas for resale for ultimate public consumption for domestic, commercial, industrial, or any other use, and to natural-gas companies engaged in such transportation or sale, but shall not apply to any other transportation or sale of natural gas or to the local distribution of natural gas or to the facilities used for such distribution or to the production or gathering of natural gas,
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> SEC. 5. (a) Whenever the Commission, after a hearing had upon its own motion or upon complaint of any State, municipality, State commission, or gas distributing company, shall find that any rate, charge, or classification demanded, observed, charged, or collected by any natural-gas company in connection with any transportation or sale of natural gas, subject to the jurisdiction of the Commission, or that any rule, regulation, practice, or contract affecting such rate, charge, or classification is unjust, unreasonable, unduly discriminatory, or preferential, the Commission shall determine the just and reasonable rate, charge, classification, rule, regulation, practice, or contract to be thereafter observed and in force, and shall fix the same by order: *Provided, however,*

That the Commission shall have no power to order any increase in any rate contained in the currently effective schedule of such natural gas company on file with the Commission, unless such increase is in accordance with a new schedule filed by such natural gas company; but the Commission may order a decrease where existing rates are unjust, unduly discriminatory, preferential, otherwise unlawful, or are not the lowest reasonable rates.

SEC. 6. (a) The Commission may investigate and ascertain the actual legitimate cost of the property of every natural-gas company, the depreciation therein, and when found necessary for rate-making purposes, other facts which bear on the determination of such cost or depreciation and the fair value of such property.

SEC. 7. (a) Whenever the Commission, after notice and opportunity for hearing, finds such action necessary or desirable in the public interest, it may by order direct a natural-gas company to extend or improve its transportation facilities, to establish physical connection of its transportation facilities with the facilities of, and sell natural gas to, any person or municipality engaged or legally authorized to engage in the local distribution of natural or artificial gas to the public, and for such purpose to extend its transportation facilities to communities immediately adjacent to such facilities or to territory served by such natural-gas company, if the Commission finds that no undue burden will be placed upon such natural-gas company thereby: *Provided*, That the Commission shall have no authority to compel the enlargement of transportation facilities for such purposes,

or to compel such natural-gas company to establish physical connection or sell natural gas when to do so would impair its ability to render adequate service to its customers.

(b) No natural-gas company shall abandon all or any portion of its facilities subject to the jurisdiction of the Commission, or any service rendered by means of such facilities, without the permission and approval of the Commission first had and obtained, after due hearing, and a finding by the Commission that the available supply of natural gas is depleted to the extent that the continuance of service is unwarranted, or that the present or future public convenience or necessity permit such abandonment.

SEC. 9. (a) The Commission may, after hearing, require natural-gas companies to carry proper and adequate depreciation and amortization accounts in accordance with such rules, regulations, and forms of account as the Commission may prescribe. The Commission may from time to time ascertain and determine, and by order fix, the proper and adequate rates of depreciation and amortization of the several classes of property of each natural-gas company used or useful in the production, transportation, or sale of natural gas. Each natural-gas company shall conform its depreciation and amortization accounts to the rates so ascertained, determined, and fixed. No natural-gas company subject to the jurisdiction of the Commission shall charge to operating expenses any depreciation or amortization charges on classes of property other than those prescribed by the Commission, or charge with respect to any class of property a per-

centage of depreciation or amortization other than that prescribed therefor by the Commission. No such natural-gas company shall in any case include in any form under its operating or other expenses any depreciation, amortization, or other charge or expenditure included elsewhere as a depreciation or amortization charge or otherwise under its operating or other expenses. Nothing in this section shall limit the power of a State commission to determine in the exercise of its jurisdiction, with respect to any natural-gas company, the percentage rates of depreciation or amortization to be allowed, as to any class of property of such natural-gas company, or the composite depreciation or amortization rate, for the purpose of determining rates or charges.

SEC. 19. (b) Any party to a proceeding under this Act aggrieved by an order issued by the Commission in such proceeding may obtain a review of such order in the circuit court of appeals of the United States for any circuit wherein the natural-gas company to which the order relates is located or has its principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within sixty days after the order of the Commission upon the application for rehearing, a written petition praying that the order of the Commission be modified or set aside in whole or in part. * * *. No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure

so to do. The finding of the Commission as to the facts, if supported by substantial evidence, shall be conclusive. * * *. The judgment and decree of the court, affirming, modifying, or setting aside, in whole or in part, any such order of the Commission, shall be final, subject to review by the Supreme Court of the United States upon certiorari or certification as provided in sections 239 and 240 of the Judicial Code, as amended (U. S. C., title 28, secs. 346 and 347).

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